

## Message Text

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ACTION EA-14

INFO OCT-01 EUR-25 ISO-00 CIAE-00 DODE-00 PM-07 H-03

INR-10 L-03 NSAE-00 NSC-10 PA-03 RSC-01 PRS-01 SPC-03

SS-15 USIA-15 ACDA-19 IO-13 AID-20 COME-00 EB-11

FRB-02 TRSE-00 XMB-07 OPIC-12 CIEP-02 LAB-06 SIL-01

OMB-01 DRC-01 SAJ-01 CEA-02 /209 W

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R 200705Z SEP 73

FM AMEMBASSY TOKYO

TO SECSTATE WASHDC 6919

INFO AMEMBASSY BERN

AMEMBASSY BONN

AMEMBASSY LONDON

AMEMBASSY PARIS

AMCONSUL HONG KONG

USLO PEKING

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PASS TREASURY AND FEDERAL RESERVE

E.O. 11652: N/A

TAGS: EFIN, CH

SUBJECT: AGREEMENTS BETWEEN JAPANESE BANKS AND PEOPLES

BANK OF CHINA

REF: STATE 182462

SUMMARY: IN AUG BANK OF TOKYO RENEGOTIATED AGREEMENT WITH  
PEOPLES BANK OF CHINA (BOC) FOLLOWING SUCCESSFUL OPERATION  
OF LAST YEAR'S AGREEMENT WHICH WAS ON ONE-YEAR TRIAL BASIS.  
DETAILS ON FINANCIAL RELATIONS BETWEEN JAPANESE BANKS AND  
BOC AND HOW YEN/REN-MIN-BI (RMB) TRANSACTIONS ARE HANDLED  
ARE DESCRIBED BELOW BASED ON CONVERSATION WITH KNOWLEDGEABLE  
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BANK OF TOKYO OFFICIAL.

1. BANK OF TOKYO WAS THE FIRST JAPANESE BANK TO NEGOTIATE AN AGREEMENT WITH BOC FOR HANDLING YEN/RMB TRANSACTIONS ON A ONE-YEAR "TRIAL" PERIOD. THEREAFTER 19 OTHER JAPANESE BANKS SIGNED VERY SIMILAR AGREEMENTS WITH BOC. BANK OF TOKYO SUCCESSFULLY RENEGOTIATED THIS AGREEMENT IN AUG 73 WHICH ELIMINATES ANY REFERENCE TO "TRIAL BASIS." THAT AGREEMENT IS AUTOMATICALLY RENEWABLE EACH YEAR UNLESS EITHER PARTY WISHES TO SEEK AMENDMENTS TO IT. BOC WILL NOT RENEGOTIATE AGREEMENTS WITH OTHER 19 BANKS WHO WILL MERELY OPERATE UNDER THE SAME PROVISIONS AS IN THE AGREEMENT WITH BANK OF TOKYO. THIS YEAR'S AGREEMENT PROVIDES FOR SETTLEMENT OF "INVISIBLES" AS WELL AS TRADE TRANSACTIONS. WHILE INTERBANK TRANSACTIONS WILL BE AT THE OFFICIAL YEN/RMB RATE, FIXED PERIODICALLY BY BOC, JAPANESE BANKS IN QUOTING RMB TO JAPANESE EXPORTERS AND IMPORTERS WILL USE AN "ARBITRATED RATE" DESCRIBED IN PARA 3 BELOW.

2. BOC SETS OFFICIAL YEN/RMB RATE WHICH USED IN ALL INTERBANK TRANSACTIONS BETWEEN BOC AND JAPANESE BANKS. RATE IS CHANGED PERIODICALLY AND NEW RATE TELEXED DIRECTLY TO EACH OF 20 PARTICIPATING BANKS. REASON FOR RATE CHANGES DUE TO ALTERATIONS IN OFFICIAL STERLING/RMB RATE, FLUCTUATIONS IN YEN, DOLLAR AND DM. BANK OF TOKYO HAS NOT BEEN ABLE TO DETERMINE SPECIFIC FORMULA BOC MAY BE USING IN SETTING YEN/RMB RATE. CURRENT RATE ABOUT Y137 PER RMB. FOR TRANSACTIONS WITH JAPANESE EXPORTERS AND IMPORTERS, BANKS DO NOT QUOTE OFFICIAL RATE BUT USE "ARBITRATED RATE" DESCRIBED IN PARA 3 BELOW. THUS, BANKS HOLDING OF RMB AS WELL AS YEN DEPOSITS OF BOC ARE SUBJECT TO SOME EXCHANGE RISK. NEVERTHELESS, BANK OF TOKYO OFFICIAL WELL-PLEASED WITH PAST EXPERIENCE. CITES THAT DURING 317 TRADING DAYS OF FIRST YEAR'S AGREEMENT ARBITRATED RATE FLUCTUATED WITHIN NARROW RANGE OF PLUS OR MINUS 3 PERCENT OF "FIXED RATE" DURING 90 PERCENT OF TIME. BANK OF TOKYO OFFICIAL CONSIDERS EXCHANGE RATE EXPOSURE TO BE QUITE ACCEPTABLE BASED ON PAST EXPERIENCE.

3. ARBITRATED RATE FOR YEN/RMB DETERMINED DAILY AS FOLLOWS:  
(A) STARTING WITH OFFICIAL STERLING/RMB RATE, THIS IS (B)  
CONVERTED INTO DOLLARS AT NEW YORK CLOSING RATE FOR STERLING  
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(REUTERS) OF PREVIOUS DAY AND THEN (C) CONVERTED INTO YEN AT TOKYO SPOT OVERNIGHT RATE DURING TRADING OF EACH MORNING. AFTER RATE HAS BEEN DETERMINED DAILY IN THIS MANNER, BANKS ADD A SPREAD ON EITHER SIDE OF Y0.65 PER RMB OR ROUGHLY 0.5 PERCENT. THESE RATES ARE QUOTED TO JAPANESE TRADERS WISHING TO MAKE OR RECEIVE PAYMENTS IN RMB.

4. EACH JAPANESE BANK MAINTAINS CURRENT DEPOSITS WITH BOC

IN RMB ON WHICH NO INTEREST IS PAID. THESE CONSIDERED WORKING BALANCES WHICH CAN OF COURSE BE REDUCED IF BANKS CONCERNED ABOUT EXCHANGE RISKS. BANK OF TOKYO OFFICIAL ESTIMATES AGGREGATE AMOUNT PERHAPS AS MUCH AS \$100 MIL. FOLLOWING NEGOTIATION OF ORIGINAL AGREEMENTS, DEPOSITS WERE BUILT UP WITH BOC BUT IN RECENT MONTHS AGGREGATE AMOUNT THOUGHT TO HAVE BEEN RELATIVELY STABLE.

5. BOC IN TURN HOLDS FREE YEN DEPOSITS WITH JAPANESE BANKS. NO INTEREST IS PAID AND IN FACT SOME BANKS REPORTED TO HAVE CHARGED NEGATIVE INTEREST IN EFFORT TO DISCOURAGE INCREASES IN THESE DEPOSITS. THIS IS BECAUSE FREE YEN DEPOSITS VERY COSTLY FOR JAPANESE BANKS AGAINST WHICH THERE IS A 50 PERCENT RESERVE REQUIREMENT WITH BOJ AS WELL AS FOREX CONTROL REQUIREMENT TO INVEST IN FOREIGN ASSETS TWICE THE AMOUNT OF ANY INCREASE IN FREE YEN DEPOSITS. (FOR FURTHER DETAILS SEE FORMER ASST FINATT WILBUR MONROE'S RECENTLY PUBLISHED BOOK, "JAPAN: FINANCIAL MARKETS AND THE WORLD ECONOMY," PAGES 64-65). BANK OF TOKYO OFFICIAL COMMENTED THAT SINCE APRIL, WHEN JAPANESE IMPORTS FROM PRC INCREASED SUBSTANTIALLY, FREE YEN DEPOSITS OF BOC HAVE INCREASED TO PERHAPS DOLLAR EQUIVALENT OF \$50 MIL.

6. FINATT, CITING FOREX CONTROL REGULATIONS, MENTIONED PARA 5 ABOVE, ASKED WHETHER JAPANESE BANKS WERE INCREASING FOREIGN ASSETS BY PLACING ADDITIONAL FUNDS DIRECTLY WITH BOC. BANK OF TOKYO OFFICIAL DENIED THIS. SAID JAPANESE BANKS NOT REPEAT NOT EXTENDING CREDITS TO OR PLACING FUNDS WITH BOC EITHER IN TOKYO OR THROUGH FOREIGN BRANCHES ABROAD. TO MEET FOREX REGULATIONS, BANKS GENERALY PLACE FUNDS IN EURODOLLAR MARKET OR PERHAPS U.S. THIS HAS BEEN EXPENSIVE IN PAST YEAR BECAUSE OF HIGH PREMIUM ON FORWARD YEN.

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7. BANK OFFICIAL HAD HEARD UNCONFIRMED RUMORS THAT BOC BRANCH IN LONDON IS DEALING DIRECTLY WITH SEVERAL LARGE FOREIGN BANKS FOR PLACEMENT OF FUNDS WITH BOC. SAID THAT BY NOT OPERATING THROUGH FOREIGN EXCHANGE DEALERS, BOC WOULD TRY TO MAINTAIN SECRECY ON VOLUME OF DEPOSITS AND OTHER INTERBANK DEALINGS. OFFICIAL ALSO REMARKED THAT FREE YEN DEPOSITS OF BOC ARE OCCASIONALLY REDUCED AS BANK WITHDRAWS FUNDS FOR CONVERSION INTO STERLING OR DM. THIS IS BECAUSE YEN IS NOT INTERNATIONAL TRADING CURRENCY.

8. JAPANESE EXPORTERS ARE EXTENDING THREE TO FIVE YEAR CREDITS TO PRC IN ORDER TO SELL CAPITAL GOODS ON DEFERRED PAYMENT BASIS. LIABILITY IS DENOMINATED IN RMB AND EXPORTERS BEAR ANY EXCHANGE RISKS. JAPANESE BANKS DO OF COURSE EXTEND YEN LOANS TO MANUFACTURERS OR TRADING COMPANIES IN CONNECTION LIMITED OFFICIAL USE

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WITH THESE SHIPPERS USANCE CREDITS. OFFICIAL ESTIMATED TOTAL VOLUME OF SUCH USANCE CREDITS CURRENTLY OUTSTANDING AT PERHAPS \$100 MIL. VOLUME IS EXPECTED TO INCREASE RAPIDLY IN VIEW OF NEGOTIATIONS NOW UNDER WAY FOR SALE OF SUBSTANTIAL VOLUME OF CAPITAL GOODS TO PRC. INGERSOLL

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